**Chapter 5 Bingham CAPITAL PROJECTS FUNDS**

The reason for creating a fund to account for capital projects is the same as the reason for creating special revenue funds—to provide a formal mechanism to enable administrators to ensure revenues and other financing sources dedicated to a certain purpose are used for that purpose and no other.

For example, grants or other resources provided by state and federal agencies to help finance capital acquisitions made by local governments necessitate the establishment of accounting and reporting procedures that can provide information showing compliance with terms of the grants. Furthermore, the use of a fund helps ensure that all required information is provided when it is needed. Also, capital projects financed through general obligation debt should be accounted for in a capital projects fund.

Capital projects funds differ from the General Fund and special revenue funds in that the latter categories have a year-to-year life, whereas capital projects funds have a project-life focus and may be in existence for several years.

Accounting for a capital project begins when a capital project or a series of related projects is legally authorized; the fund is closed when the project or series is completed.

Appropriation accounts need not be used because the legal authorization to engage in the project is in itself an appropriation of the total amount that may be obligated for the construction or acquisition of the capital asset specified in the project authorization. Estimated revenues need not be recorded because few contractors will start work on a project until financing is ensured through the sale of bonds or the receipt of grants or gifts. To provide control over the issuance of contracts and purchase orders, which may be numerous and which may be outstanding for several years in construction projects, it is recommended that the encumbrance procedure be used.

**Since the purpose of the capital projects fund is to account for the receipt and expenditure of financial resources earmarked for capital projects, its balance sheet reports only financial resources and the liabilities to be liquidated by those resources. Neither the capital assets acquired nor any long-term debt incurred for the acquisition is recorded in a capital projects fund; these items are recorded in the governmental activities general ledger at the government-wide level.**

GASB standards require the use of the same basis of accounting for capital projects funds as for the other governmental fund types.

Proceeds of debt issues should be recorded as Proceeds of Bonds or Proceeds of Long-Term Notes rather than as Revenues, and they should be reported in the Other Financing Sources section of the statement of revenues, expenditures, and changes in fund balance.

Similarly, tax revenues raised by the General Fund or a special revenue fund and transferred to a capital projects fund are recorded as Inter-fund Transfers In and reported in the Other Financing Sources section of the operating statement.

Taxes raised specifically for a capital projects fund would be recorded as revenues of that fund. The same holds true for special assessments to be used for the construction of assets that will be of particular benefit to certain property owners. Grants, entitlements, or shared revenues received by a capital projects fund from another government are considered revenues of the capital projects fund. Interest earned on investments of the capital projects fund is also considered revenue if the interest is available for expenditure by the capital projects fund. If, by law, the interest must be used for service of general long-term capital debt, the interest should be transferred to the appropriate debt service fund.

**City Hall Annex Construction Fund and Governmental Activities at the Government-wide Level**

During fiscal year 2016, the voters of the City of Bingham approved the issuance of three (3) percent tax-supported serial bonds in the face amount of $7,500,000 to construct and equip an annex to the City Hall. The bonds are to mature in blocks of $375,000 every six months over a 10-year period commencing January 1, 2018. If you need help with accounting for bond transactions, let me know and I will send you a video on them.

No formal entry is required to record voter and town council approval. - Proceeds of debt issues should be recognized by a capital projects fund at the time the issue is sold rather than the time it is authorized because authorization of an issue does not guarantee its sale.

**Required**

1. Prepare general journal entries as necessary to record the following transactions in the general journals of the **City Hall Annex Construction Fund** and, if applicable, in the governmental activities general journal at the government-wide level. Do *not* record entries at this time in any other affected funds; those entries will be made in later chapters of this cumulative problem that cover those funds. Use account titles listed under the drop-down menu. Be sure the year **2017** is selected from the drop-down menu and the appropriate paragraph number shown in bold-face font below is in the **[Transaction Description]** box.
2. **[Para. 5-a-1]** On the first day of the 2017 fiscal year (January 1, 2017), the bond issue was sold at 101. Cash in the face amount of the bonds, $7,500,000, was deposited in the City Hall Annex Construction Fund; the premium was deposited in the debt service fund, as required by state law.

**Required:** Record these transactions in the City Hall Annex Construction Fund and governmental activities journals. (Hint: In addition to recording the liability for bonds payable in the governmental activities journal, you should record the premium on the bonds payable in the governmental activities general journal.) Wait until instructed in Chapter 6 to make the corresponding entry in the debt service fund.



These entries show the contrast between how the bond issue is recorded in the general journals for the capital projects fund and governmental activities at the government-wide level.

Since the bond issue increases current financial resources in the capital projects fund, the credit is to Other Financing Sources—Proceeds of Bonds rather than to a liability account. The long-term liability is recorded in the governmental activities general journal as a credit to Bonds Payable, reflecting the economic resources measurement focus used at the government-wide level.

1. **[Para. 5-a-2]** The city invested $5,000,000 of the bond proceeds in 90-day notes to earn interest until the bond proceeds are needed.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals.



1. **[Para. 5-a-3]** The City Hall Annex Construction Fund purchased land for the annex for $500,000. This amount was vouchered and is credited to Vouchers Payable. As you have guessed by now, governments use vouchers payable instead of accounts payable.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. In the governmental activities general journal at the government-wide level, this purchase should be debited to Land. (Note: **This transaction was not encumbered since the amount is not an estimate but the purchase price**.)



1. **[Para. 5-a-4]** A contract for architectural services was signed at an **estimated** amount of $325,000 for the design of the City Hall Annex.

Accounting will follow the **encumbrances** approach wherein **estimated** amounts are encumbered until such time as the actual invoices are received. Then the estimated encumbrance is reversed, the actual amount recorded as a payable. The payable is then debited when paid and cash is credited.

**Required:** Record the encumbrance in the City Hall Annex Construction. This transaction has no effect at the government-wide level.



1. **[Para. 5-a-5]** Legal and other capitalizable costs of the bond issue were vouchered in the amount of $150,000.

**NOTE:** A Capital Project Fund does not use Construction in Progress but Construction Expenditures; whereas the Govt-Wide uses Construction in Progress.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. (Note: This transaction was not encumbered because the amount are known and not estimates.)



1. **[Para. 5-a-6] Preliminary** plans were received (related to the contract signed in paragraph 5-a-4) for which architectural fees of $95,000 were vouchered.

**Required:** Eliminate a portion of the encumbrance and record a Vouchers Payable liability in the City Hall Annex Construction Fund and governmental activities journals, as appropriate.



1. **[Para. 5-a-7]** Construction bids were opened and analyzed. A contract was signed with the firm that submitted the winning bid of $6,000,000. **A provision of the contract permits the city to withhold 5 percent of payment pending final acceptance of the completed project.**

**Required:** Record the signing of the contract in the City Hall Annex Construction Fund general journal. This transaction has no effect at the government-wide level.



At this time, take a look at the encumbrances outstanding and the vouchers payable in relation to the cash and investments through the Pre Closing Trial Balance for the City Hall Annex. Can you see how the government would be able to determine it has not overspent its funding?

1. **[Para. 5-a-8]** Vouchers payable were recorded in the amount of $220,000 for the final architectural plans and specifications for the construction project (see para. 5-a-4).

**Required: Eliminate the remaining encumbrance** for the architectural services and record a Vouchers Payable liability in the City Hall Annex Construction Fund and governmental activities journals, as appropriate.



View the Annex Pre-Closing Trial Balance and see the changes in the encumbrances balances after these journal entries.

1. **[Para. 5-a-9]** The 90-day notes matured, paying $37,500 in interest (see para. 5-a-2).

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. The interest should be recorded as general revenue in the governmental activities journal.



1. **[Para. 5-a-10]** The contractor submitted a billing for $3,000,000. This amount was recorded as a contract payable.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals.



Take a look at the annex fund pre-closing trial balances and see how the composition of the encumbrances and payable are changing.

1. **[Para. 5-a-11]** The contractor’s billing (see para. 5-a-10) was paid, less a 5 percent retained percentage.

It is common to require contractors on large-scale contracts to give performance bonds, providing for indemnity to the government for any failure on the contractor's part to comply with terms and specifications of the agreement. Before final inspection of a project can be completed, the contractor may have moved its work force and equipment to another location, thus making it difficult to remedy possible objections to the contractor's performance. Also, the shortcoming alleged by the government may be of a controversial nature with the contractor unwilling to accede to the demands of the government. Results of legal action in such disagreements are not predictable.

To provide more prompt adjustment on shortcomings not large or convincing enough to justify legal action and not recoverable under the contractor's bond, as well as those the contractor may admit but not be in a position to rectify, it is common practice to withhold a portion of the contractor's payment until final inspection and acceptance have occurred. The withheld portion is normally a contractual percentage of the amount due on each segment of the contract.

The retained percentage account is used when payment is made not before.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals.



1. **[Para. 5-a-12]** All pending vouchers were approved and paid.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals.



1. **[Para. 5-a-13]** Furniture and equipment for the annex were ordered at an **estimated** total cost of $465,000.

**Required:** Record this transaction in the City Hall Annex Construction Fund. It has no effect on the governmental activities general journal.



1. **[Para. 5-a-14]** The contractor completed construction, submitted the final bill, and requested payment of the balance due. A liability was recorded in the amount of $3,100,000.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. The encumbrance account should be reduced by the remaining $3,000,000 construction contract balance.



Take a look at the annex fund pre-closing trial balances and see how the composition of the encumbrances and payable are changing. The only encumbrance at this point is for the furniture and equipment from 5-a-13.

1. **[Para. 5-a-15]** After final inspection, a final payment was made to the contractor, including the amount retained in para. 5-a-11.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals.



1. **[Para. 5-a-16]** Furniture and equipment were received (see para. 5-a-13) at a total cost of $465,500. Invoices were vouchered for payment.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. This amount exceeds the city’s capitalization threshold, so Equipment should be debited.



Take a look at the annex fund pre-closing trial balances and see how the composition of the encumbrances and payable have changed. There are no more encumbrances.

1. **Para. 5-a-17]** The City Hall Annex Construction Fund paid all outstanding liabilities on December 31, 2017.

**Required:** Record this transaction in both the City Hall Annex Construction Fund and governmental activities general journals. Total construction costs for the City Hall Annex Construction Project should be capitalized in the Buildings account in governmental activities.

View **Govt Wide** activities pre-closing trial balance before this entry to see the amount in construction in progress.

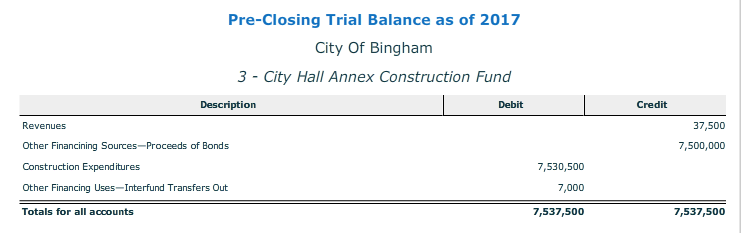


1. **[Para. 5-a-18]** Remaining cash in the City Hall Annex Construction Fund was transferred to the debt service fund. View Gen Fund pre-closing trial balance. What amount remains in cash?

**Required:** Record this transaction in the City Hall Annex Construction Fund. Do not record the transfer in the debt service fund until you are instructed to do so in Chapter 6. This transaction involves two governmental funds, thus it has no effect on the governmental activities general journal.



1. At this juncture, your pre-closing trial balance should look like this.



For the City Hall Annex Construction Fund only, prepare year-end closing entries for 2017 and post them to the fund’s general ledger. (Note: You must click on the box for **[Closing Entry]** to check mark it;“Closing Entry” will appear in the **[Transaction Description]** box for the account being closed. Be sure the check mark is present for each account being closed.) Click **[Post Entries]** to post the closing entry. Closing entries will be made in the governmental activities general journal in Chapter 9 of this cumulative problem. Ignore those entries for now.



**Note:** If you prepare a Gen Fund post closing trial balance, a report cannot be produced since there are no remaining amounts.

**Before closing the *City of Bingham,* click on [File], and [Save/Save As] to save your work.** If you close the file by clicking on the [**X**] box you will be asked if you want to save your changes before closing.

1. **Refer to list of documents to be graded.** Annex Fund – all general ledger balances should be zero.
2. Review the statement of revenues, expenditures, and changes in fund balances for the City Hall Annex Construction Fund for the year ended December 31, 2017. (Note: A balance sheet is not required since the capital project fund was closed prior to end of FY 2017.)

You will prepare a similar one for the Smithville project for the Street Improvement Capital Projects fund.

